IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF IOWA
WESTERN DIVISION

HINKEL EXCAVATION AND CONSTRUCTION, INC., and CURTIS HINKEL, Plaintiffs, vs. CONSTRUCTION EQUIPMENT INTERNATIONAL, LTD., CASE CREDIT CORPORATION, and AMERILEASE CORP., Defendants.	No. C00-4090 **MEMORANDUM OPINION AND ORDER REGARDING DEFENDANTS' MOTION TO STAY**

This matter comes before the court pursuant to the August 25, 2000, Motion to Stay (#3)[1] filed by defendants, Case Credit Corporation ("Case") and AmeriLease Corp. ("AmeriLease"). Specifically, defendants ask that the court stay the present federal court proceeding in deference to a previously filed state court proceeding in California.

I. INTRODUCTION

A. Factual Background

The facts giving rise to this dispute stem from a series of transactions that occurred on May 18, 1999. On that date, AmeriLease and Hinkel Excavation and Construction, Inc., entered into a written lease agreement wherein AmeriLease agreed to lease a used 1997-1432 Pav-Saver Maxi-Pav HD Slipform Paver to Hinkel Excavation and Construction, Inc.

[1] On August 25, 2000, defendant AmeriLease joined in Case's Motion to Stay.

Concurrent with the signing of the lease, Curtis Hinkel executed a personal, unconditional guaranty for the extension of said credit. Later that same day, AmeriLease assigned the lease, for consideration, to Case. Case had already approved the lease for the concrete paver to Hinkel Excavation and Construction, Inc. After receiving the assignment of the lease, Case paid the sum of $120, 450.00 to the vendor of the equipment, Construction Equipment International, Inc. ("CEI"), on May 21, 1999.

Hinkel Excavation and Construction, Inc., gave $10,000.00 to CEI as a down payment for the paver and began making the required monthly payments of $3,045.00 to Case under the terms of the lease. However, the paver never arrived. On June 18, 1999, the Hinkels stopped making the monthly payments to Case pursuant to the lease. The paver, for reasons unknown, wound up in Mexico.

B. Procedural Background

On March 24, 2000, Case, as Delaware corporation, filed a lawsuit against AmeriLease, a California Corporation, in the Superior Court of the State of California for the County of Orange. Thereafter, on May 15, 2000, AmeriLease filed a cross-complaint against Case and other parties, including Hinkel Excavation & Construction, Inc., an Iowa corporation, and Curtis Hinkel, a resident of Iowa (collectively referred to as the "Hinkels"). On July 20, 2000, the Hinkels filed a declaratory judgment action in the Iowa District Court for Woodbury County against these defendants seeking rescission of three written contracts. The Hinkels instituted the Iowa state suit allegedly within two days of being served with AmeriLease's cross-complaint. On August 25, 2000, Case removed the action from Iowa state court to this court pursuant to 28 U.S.C. 1441(a). AmeriLease joined in the removal. On that same date, defendants filed the present motion to stay.

Defendants Case and AmeriLease moved to stay this proceeding based on the parallel proceeding in California Superior Court. Relying primarily on *Brillhart v. Excess Ins. Co.*

of America, 316 U.S. 491 (1942), and to a lesser extent on *Colorado River Water Conservation District v. United States*, 424 U.S. 800 (1976) and *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.* 460 U.S. 1 (1980), defendants set forth several reasons in support of their motion to stay: that there is a currently pending, and previously filed, state court action in California involving the same parties that has raised or will raise the same issues raised in the present federal claim; that the scope and nature of the California action is the same as the present federal one; that the California action has made substantial progress, including written discovery, depositions and a status conference; that the California court has also started to address the substantive issues involved in the claim as a result of Case's demurrer to the claims filed against it in AmeriLease's cross-complaint; that the Hinkels can raise as an affirmative defense in the California state court action any breach of contract or failure to perform by any of the other parties that may justify rescission or non-payment by them; that the Hinkels' claim for declaratory judgment is essentially reactive in nature to the California lawsuit; that no issue of federal law is involved and a parallel state court proceeding does exist; and that it is in the interest of judicial economy and efficient judicial administration to stay this action in deference to the previously filed California action.

In contrast, the Hinkels assert that a federal court presented with the question of whether to stay a case based on the pendency of a parallel state court proceeding must retain a strong presumption that it will exercise jurisdiction. In direct contrast to the defendants, plaintiffs rely primarily on *Colorado River* and *Moses H. Cone*, and to a lesser extent on *Brillhart*, arguing that there is no parallel state court proceeding because the California state court does not have jurisdiction over them. The Hinkels also argue the following: that the defendants have not shown that "exceptional circumstances" exist, which would warrant such a stay; that the defendants have failed to demonstrate that any significant proceedings have taken place in the California state action; that only a limited amount of discovery has

been exchanged between the parties; and that defendants have not shown that the issues would be better resolved in the pending state California court proceeding.

On November 7, 2000, the court heard oral arguments on the defendants' Motion to Stay. Plaintiffs Hinkels were represented by Gregory N. Lohr of Baron Sar Goodwin Lohr & Horak, Sioux City, Iowa. Defendant Case was represented by Thomas H. Walton of Nyemaster Goode Voigts West Hansell & O'Brien, P.C., Des Moines, Iowa. Defendant AmeriLease was represented by Nicholas Critelli, III, Des Moines, Iowa.

II. LEGAL ANALYSIS

A. Law Governing the Stay

This case was initially filed in Iowa District Court for Woodbury County as a state court declaratory judgment action seeking rescission of the three contracts. The case was then removed to this court by virtue of 28 U.S.C. § 1441. This framework raises the question of whether federal or state law applies to the determination of the motion to stay presently before the court. When a declaratory judgment action filed in state court is removed to federal court, that action is in effect converted into one brought pursuant to the federal Declaratory Judgment Act, 28 U.S.C. § § 2201, 2202. *See Toops v. United States Fidelity & Guar. Co.*, 871 F. Supp. 284, 287 & n. 2 (S.D. Tex. 1994) ("Plaintiffs . . . brought suit in the 149th Judicial District Court of Brazoria County, Texas, claiming breach of contract and seeking a declaratory judgment of their rights under the Texas Declaratory Judgment Act. . . . Because this case was later removed to this Court, Plaintiff's Declaratory Judgment Act claim is now properly asserted under 28 U.S.C. § § 2201 and 2202.), rev'd on other grounds *sub nom. Toops v. Gulf Coast Marine Inc.*, 72 F.3d 483 (5th Cir. 1996); *see also DeFeo v. Procter & Gamble Co.*, 831 F. Supp. 776, 779 (N.D. Cal. 1993) ("[T]he Declaratory Judgment Act is implicated even in diversity cases, whether an action is originally filed in federal court or is properly removed there by defendant.").

Relief under the Declaratory Judgment Act is procedural in nature. *Fischer & Porter Co. v. Moorco Int'l, Inc.*, 869 F. Supp. 323, 326 (E.D. Pa. 1994); *Nationwide Mut. Ins. Co. v. Welker*, 792 F. Supp. 433, 439-40 (D. Md. 1992). Thus, federal law governs whether relief may be had under the Declaratory Judgment Act and whether the motion to stay proceeding should be granted even when declaratory relief is originally sought under state law. *Haagen-Dazs Shoppe Co. v. Born*, 897 F. Supp. 122, 126 n. 2 (S.D.N.Y. 1995); *see Quality King Distributors, Inc. v. KMS Research Inc.*, 946 F. Supp. 233, 236 (E.D.N.Y. 1996).

B. Jurisdiction Under The Declaratory Judgment Act

As indicated previously, both parties analyze whether the court should stay this federal proceeding in deference to the state proceeding in California under both the *Colorado River* doctrine and the *Brillhart* doctrine. The Supreme Court in *Wilton v. Seven Falls Co.*, 515 U.S. 277 (1995), however, held that the discretionary standard set forth in *Brillhart*, not the *Colorado River* "exceptional circumstances" test, governs a district court's decision to stay a declaratory judgment action during the pendency of parallel state court proceedings. *See Wilton*, 515 U.S. at 282-83; *Prudential Ins. Co. v. Doe*, 140 F.3d 785, 789 (8th Cir. 1998) (stating that *Wilton* makes clear that the exceptional circumstances test of *Colorado River* and *Moses H. Cone* does not control in declaratory judgment actions; rather the *Brillhart* factors do); *see also Black Sea Investment, Ltd. v. United Heritage Corp.*, 204 F.3d 647, 652 (5th Cir. 2000) ("*Brillhart* abstention is applicable when a district court is considering abstaining from exercising jurisdiction over a declaratory judgment action. In contrast, when actions involve coercive relief the trial court must apply the standards enunciated by the Court in *Colorado River*.") (internal quotation marks and citation omitted); *Youell v. Exxon Corp.*, 74 F.3d 373, 375-76 (2d Cir. 1996) (same). The court finds that the discretionary standard enunciated in *Brillhart* is applicable in this case

because the Hinkels' complaint seeks a declaratory judgment, and the further relief they seek is the subject of the declaratory judgment action, *to wit*: rescission of the three contracts.[2] *See Coregis Ins. Co. v. Frank, Seringer & Chaney, Inc.*, 993 F. Supp. 1092, 1095 (N.D. Ohio 1997) (applying the discretionary standard enunciated in *Brillhart* to declaratory judgment seeking rescission); *accord Gatewood Lumber, Inc v. Travelers Indemnity Co.*, 898 F. Supp. 364, 366 (S.D. W.Va. 1995).[3] Indeed, the relief that the

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[2]Congress has provided for declaratory judgments by the federal courts through two provisions of the Declaratory Judgment Act, which state, in pertinent part, the following:

> § 2201. Creation of remedy
> (a) In a case of actual controversy within its jurisdiction, . . . any court of the United States, upon the filing of an appropriate pleading, may declare the rights and other legal relations of any interested party seeking such declaration, whether or not further relief is or could be sought. Any such declaration shall have the force and effect of a final judgment or decree and shall be reviewable as such.
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> * * * * * *
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> § 2202. Further relief
> Further necessary or proper relief based on a declaratory judgment or decree may be granted, after reasonable notice and hearing, against any adverse party whose rights have been determined by such judgment.

28 U.S.C. § § 2201(a), 2202. The first provision of the Declaratory Judgment Act, § 2201, provides for the specific declaratory relief the Hinkels seek. Furthermore, § 2202 provides for the further relief of rescission that might be appropriate as a result of the requested declarations. Thus, rescission is an available remedy under the Declaratory Judgment Act.

[3]Actions by insurers seeking the rescission of an insurance policy have been brought as declaratory judgment actions in several courts. *See*, *e.g.*, *Allstate Ins. Co. v. Springer*, 269 F.2d 805 (6th Cir. 1959); *Paul Revere Life Ins. Co. v. Fima*, 105 F.3d 490 (9th Cir. 1997); *Home Ins. Co. v. Dunn*, 963 F.2d 1023 (7th Cir. 1992); *State Farm Mut. Auto. Ins. Co. v. Armstrong*, 949 F.2d 99 (3rd Cir. 1991); *Bankers Sec. Life Ins. Soc. v. Kane*, 885 F.2d 820 (11th Cir. 1989); *North River Ins. Co., Inc. v. Stefanou*, 831 F.2d 484 (4th Cir. 1987); *Bankers Life & Cas. Co. v. Namie*, 341 F.2d 187 (5th Cir. 1965); *Glenn v. State* (continued…)

Hinkels seek—rescission—is so closely tied to the interpretations of the three written contracts that the resolution of those claims is dependent on the outcome of the declaratory judgment claim. *See Gatewood,* 898 F. Supp. at 366 ("Although the parties in the instant action are seeking substantive relief in addition to declaratory judgment, the substantive claims are so closely tied to the interpretation of the insurance contract the resolution of those claims is dependent on the outcome of the declaratory judgment claims."); *Coregis Ins. Co.,* 993 F. Supp. at 1092 (applying *Brillhart* factors instead of *Colorado River* factors to plaintiff's declaratory judgment/rescission action in determining whether to stay the federal court proceeding in deference to state court proceeding). *But see First State Ins. Co. v. Callan Assoc., Inc.,* 113 F.3d 161, 163 (9th Cir. 1997) (stating that an action to rescind an insurance contract is distinct from an action merely to interpret an insurance contract and, therefore, the *Colorado River* factors were applicable to the motion to stay); *Government Employees Ins. Co. v. Dizol,* 133 F.3d 1220, 1225 (9th Cir. 1998) ("[W]hen other claims are joined with an action for declaratory relief (e.g. bad faith, breach of contract, breach of fiduciary duty, rescission, or claims for other monetary relief), the district court should not, as a general rule, remand or decline to entertain the claim for declaratory relief."). In this case, the Hinkels have not asserted any claims for monetary relief. Rather, the Hinkels have only requested equitable relief, namely, that the written contracts be cancelled; that they be released from the apparent obligations thereunder; that they have judgment against the defendants for the amounts paid under the terms of the written contracts with interest from the date of payments; and that the court do full equity to all of the parties and give such relief as may be equitable and appropriate in the premises. In so doing, the Hinkels' claims for rescission seek the same relief as their

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[3](…continued)
Farm Mut. Auto. Ins. Co., 341 F.2d 5 (10th Cir. 1965).

declaratory judgment claim. Accordingly, because the Hinkels' declaratory judgment claim regarding the three written contracts is at the heart of this case, and because rescission of the three written contracts is dependent on the outcome of the declaratory judgment claim, the court will apply the *Brillhart* factors.[4]

1. Brillhart factors

Brillhart discussed a district court's discretion with respect to actions for declaratory judgment:

> [o]rdinarily it would be uneconomical as well as vexatious for a federal court to proceed in a declaratory judgment suit where another suit is pending in a state court presenting the same issues, not governed by federal law, between the same parties. Gratuitous interference with the orderly and comprehensive disposition of a state court litigation should be avoided.

Brillhart, 316 U.S. at 495; *Wilton*, 515 U.S. at 283 (stating that "at least where another suit involving the same parties and presenting the opportunity for ventilation of the same state law issues is pending in state court, a district court might be indulging in 'gratuitous interference' if it permitted the declaratory action to proceed.") (internal citation omitted). In considering whether to proceed, *Brillhart* directed a district court to ascertain "whether the questions in controversy between the parties to the federal suit, . . . which are not foreclosed under the applicable substantive law, can better be settled in the proceeding pending in the state court." *Brillhart*, 316 U.S. at 495. *Brillhart* explained:

> Where a district court is presented with a claim such as was made here, it should ascertain whether the questions in

[4]On August 31, 2000, the Hinkels filed a Motion for Speedy Hearing pursuant to Rule 57 of the Federal Rules of Civil Procedure, asserting that Rule 57, captioned "Declaratory Judgments," provides that the court may order a speedy hearing of an action for a declaratory judgment and may advance it on the calendar. (#11). Thus, the plaintiffs characterize the present action as a declaratory judgment action, seeking equitable as well as declaratory relief.

> controversy between the parties to the federal suit, and which are not foreclosed under the applicable substantive law, can better be settled in the proceeding pending in the state court. This may entail inquiry into the scope of the pending state court proceeding and the nature of defenses open there. The federal court may have to consider whether the claims of all parties in interest can satisfactorily be adjudicated in that proceeding, whether necessary parties have been joined, whether such parties are amenable to process in that proceeding, etc.
>
> We do not now attempt a comprehensive enumeration of what in other cases may be revealed as relevant factors governing the exercise of a district court's discretion.

Brillhart, 316 U.S. at 493-97 (citations omitted). *Wilton* reiterates the propriety of this analysis. 515 U.S. at 282-83. *See also Government Employees Insurance Co. v. Dizol*, 133 F.3d 1220, 1225 (9th Cir. 1998) (en banc) ("The *Brillhart* factors remain the philosophic touchstone for the district court. The district court should avoid needless determination of state law issues; it should discourage litigants from filing declaratory actions as a means of forum shopping; and it should avoid duplicative litigation. If there are parallel state proceedings involving the same issues and parties pending at the time the federal declaratory action is filed, there is a presumption that the entire suit should be heard in state court. The pendency of a state court action does not, of itself, require a district court to refuse federal declaratory relief. Nonetheless, federal courts should generally decline to entertain reactive declaratory actions.") (citations omitted)

The Eighth Circuit Court of Appeals has held that the decision to abstain does not avail itself of a strict rule of law, but is based on the circumstances, controlled by the trial court's discretion. *Aetna Cas. and Surety Co. v. Jefferson Trust and Savings Bank of Peoria*, 993 F.2d 1364 (8th Cir. 1993). The Eighth Circuit Court of Appeals has further held that where the crux of the litigation lies in the application of a state statute, the district court was within its "unique and substantial discretion" to abstain and allow the state court's to pronounce on constitutional challenges to the state statute. *Horne v. Firemen's*

Retirement System of St. Louis, 69 F.3d 233, 236 (8th Cir. 1995).

In *Int'l Assoc. of Entrepreneurs of America v. Angoff*, 58 F.3d 1266 (8th Cir. 1995), the Eighth Circuit Court of Appeals cautioned that a sequence of events wherein a party sues in state court and the defending party subsequently asks for declaratory judgment on the same matters "alerts us to be on guard." *Id.* at 1270. "The Declaratory Judgment Act is not to be used either for tactical advantage by litigants or to open a new portal of entry to federal courts for suits that are essentially defensive or reactive to state actions." *Id.* "More specifically, the Declaratory Judgment Act is not to be used to bring to the federal courts an affirmative defense which can be asserted in a pending state action." *Id.* In *Angoff*, abstention was favored after the declaratory judgment plaintiff had tried and failed to remove the state case, and was held to be attempting to improperly gain access to federal court. Similarly, the Eighth Circuit Court of Appeals in *BASF Corp. v. Symington*, 50 F.3d 555 (8th Cir. 1995), stated that courts should look carefully to ensure that a state-court plaintiff was not being wrongfully denied his choice of forum. *BASF*, 50 F. 3d at 558. The *BASF* court, however, further stated there is "no blanket prohibition on raising affirmative defenses by declaratory action." *Id.*[5] Indeed, "where a declaratory plaintiff raises chiefly an affirmative defense, and it appears that granting relief could effectively deny an allegedly injured party its otherwise legitimate choice of the forum and time for suit, no declaratory judgment should issue." *Id.* at 559. Additionally, the court held that the factors of who filed first, and which case has made more progress, are not dispositive. *Id.*

Accordingly, this court must inquire into "whether the questions in controversy between the parties to [this] suit . . . can better be settled in the proceeding pending in the

[5]Although the *BASF* court utilized the incorrect "extraordinary circumstances" test, enunciated in *Colorado River*, in determining whether a district court should abstain from exercising jurisdiction over a declaratory judgment action, *see Wilton*, 515 U.S. at 288, several factors remain the same.

state court," *Brillhart*, 316 U.S. at 495, including inquiry into the scope of the pending state court proceeding" and consideration of "whether the claims of all parties in interest can satisfactorily be adjudicated in that proceeding, whether necessary parties have been joined, whether such parties are amenable to process in that proceeding, etc." *Id.*

2. Application of Brillhart factors

The complaint filed by the Hinkels in the Iowa District Court for Woodbury County seeks a declaration that all three written contracts—namely, the Proposal/Agreement, the Finance Lease Agreement, and the Guaranty—be rescinded and that the Hinkels be released from the apparent obligations thereunder. In doing so, the Hinkels' complaint seeks to have this court declare the rights, status and legal relations of the parties with respect to the three written contracts. However, because these claims derive from the three written contracts, and because no substantive federal law is involved, the state court in California Superior court seems better situated to resolve these issues. Indeed, many of the same issues and underlying facts are present in the state proceedings. Moreover, the Hinkels have not informed the court of any impediment they would encounter to raising the same issues on which it seeks this court's intervention as defenses in the state court action. Consequently, the court finds that the claims of all the parties in interest may be adjudicated satisfactorily in the state proceeding.

III. CONCLUSION

Therefore, the court concludes that this action will be, and hereby is, **conditionally stayed**, unless or until the Superior Court in California rules that it does not have jurisdiction over the Hinkels. In the event the California Superior Court determines that it does not have jurisdiction over the Hinkels, the Hinkels are free to file a motion asking that the court lift the stay. Because this action is stayed, plaintiffs' Motion for Summary Judgment and Motion for a Speedy Hearing are **denied as moot**.

IT IS SO ORDERED.

DATED this 20th day of November, 2000.

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MARK W. BENNETT
CHIEF JUDGE, U. S. DISTRICT COURT
NORTHERN DISTRICT OF IOWA